

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 00-15**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Application of the single article limitation on local option tax to the sales of computer software maintenance agreements.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the department by the taxpayer. The rulings herein are binding upon the Department and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time.

Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[TAXPAYER] is engaged in the business of selling packaged computer software products and maintenance agreements to customers in Tennessee. The maintenance agreements include upgrades and phone support which are priced as one item. The phone support is not listed separately from the upgrades. When the customer initially purchases the software, the accompanying maintenance is separately invoiced as one price,

regardless of the number of programs purchased. When the Taxpayer's customers purchase the optional yearly renewal of their maintenance agreement, the maintenance agreement are separately invoiced by product.

QUESTION

Does the "single article" limitation on local option tax apply to the purchase of computer software maintenance agreements?

RULING

No.

ANALYSIS

Pursuant to T.C.A. § 67-6-702(a)(1) local governments are authorized to levy privilege taxes on the same transactions and in the same manner as state sales and use taxes are imposed. Local governments are, however, limited to taxing the first \$1,600 on the sale or use of any single article of tangible personal property. A "single article" is "that which is regarded by common understanding as a separate unit exclusive of any accessories, extra parts, etc., and that which is capable of being sold as an independent unit or as a common unit of measure, a regular billing or other obligation. Such independent units sold in sets, lots, suites, etc., at a single price shall not be considered a single article." T.C.A. § 67-6-702(d).

TENN. COMP. R. & REGS. 1320-5-2-.06 further describes a single article as follows:

(2) A single article of personal property shall mean that which is regarded by common understanding as a separate unit exclusive of any accessories, extra parts, etc. and is capable of being sold as an independent unit or as a common unit of measure, a regular billing, or other obligation. Such independent units sold in sets, lots, suits, etc., at a single price shall not be considered a single article. Parts or accessories for automobiles, tractors, and other similar items that are installed at the factory and delivered with the unit as original equipment shall be treated as a part of the unit.

Software is considered tangible personal property for sales and use tax purposes. T.C.A. § 67-6-102(25)(B). Charges for warranty or service contracts warranting the repair or maintenance of tangible personal property, however, are taxable services. T.C.A. § 67-6-102(24)(F)(ix). The Taxpayer's maintenance agreements fall within the parameters of T.C.A. § 67-6-102(24)(F)(ix) and are thus a taxable service.

The single article cap does not apply to the sale of a taxable service. See, T.C.A. § 67-6-701(a)(1) (which provides that the single article cap only applies to the sale of single articles of personal property). Even though the maintenance provided by the Taxpayer consists of both upgrades and telephone support, together they constitute a service

agreement. Therefore, the single article cap does not apply to the Taxpayer's sale of its maintenance agreements, either with the initial sale or with the optional renewals.

Steven B. McCloud
Tax Counsel

APPROVED: Ruth E. Johnson
Commissioner

DATE: 6/30/00